No. 15888 ✓

See: Vol. 3063

United States Court of Appeals

For the Ninth Circuit

COMMISSIONER OF INTERNAL REVENUE,

Petitioner,

vs.

FRANK W. BABCOCK,

Respondent.

Transcript of Record

Petition to Review a Decision of the Tax Court of the United States

Phillips & Van Orden Co., 4th & Berry, San Francisco, Calif.—3-28-58

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italic; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in italic the two words between which the omission seems to occur.]

APPEARANCES

HON. CHARLES K. RICE,
Asst. U.S. Attorney General;

JOHN N. STULL,
Acting Asst. Attorney General,
Tax Division, Dept. of Justice,
Washington 25, D. C.,

For the Petitioner.

AUSTIN CLAPP,
1780 Portola Road,
Woodside, California,

For the Respondent.

The Tax Court of the United States

Docket No. 55993

FRANK W. BABCOCK,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

DOCKET ENTRIES

1955

Jan. 18—Petition received and filed. Taxpayer notified. Fee paid.

Jan. 20—Copy of petition served on General Counsel.

Jan. 18—Request for Circuit hearing in Los Angeles, Calif., filed by taxpayer. 1/26/55—Granted.

Mar. 11—Answer filed by General Counsel.

Mar. 16—Copy of answer served on Taxpayer—Los Angeles, Calif.

1956

Oct. 19—Hearing set Jan. 7, 1957—Los Angeles, Calif.

Dec. 13—Entry of appearance of Austin Clapp, as counsel, filed.

1957

Jan. 9—Trial had before Judge Atkins, case submitted, Stipulation of Facts, (2 sets), Exhibits 1-A thru 6-F, filed at hearing. Briefs due 3/11/57; Replies due 4/10/57.

1957

Jan. 24—Transcript of Hearing 1/10/57 filed.

Mar. 11—Brief filed by Respondent.

Mar. 12—Motion for extention of time to April 1, 1957, to file brief, and to May 1, 1957, to file reply brief, filed by petitioner. 3/12/57—Granted. Served 3/15/57.

Apr. 3—Brief filed by petitioner. Served 4/3/57.

May 1—Reply Brief filed by petitioner. Served 5/2/57.

June 28—Opinion rendered—Judge Atkins—Decision will be entered under Rule 50. Served 6/30/57.

Aug. 5—Computation filed by petitioner. Served Aug. 6, 1957.

Aug. 6—Hearing set Sept. 11, 1957, Rule 50. Served Aug. 6, 1957.

Aug. 23—Respondent's computation filed. Served 8/27/57.

Aug. 26—Hearing set Sept. 11, 1957, under Rule 50. Served 8/27/57.

Sept. 4—Decision entered—Judge Atkins—Div. 7. Served 9/5/57.

Sept. 6—Agreement to Respondent's computation filed by Petitioner.

Nov. 25—Petition for review by U. S. Court of Appeals, Ninth Circuit, filed by Respondent.

Nov. 25—Statement of Points filed by Respondent.

Dec. 10—Notice of filing petition for review and statement of points with proof of service thereon filed.

1957

Dec. 24—Motion to extend time to and including 2/23/58 for filing record on review and docketing the petition for review filed. Served 12/27/57.

Dec. 26—Order, extending time for filing the record on review and docketing petition for review in the U.S.C.A., 9th Circuit, to 2/23/58, entered. Served 12/27/57.

1958

Jan. 29—Designation of contents of record on review with proof of service thereon filed.

[Title of Tax Court and Cause.]

OPINION

Filed June 28, 1957.

Section 112(f), Internal Revenue Code of 1939—Involuntary Conversion—The property of the petitioner was condemned by the Sate of California under its power of eminent domain. Part of the award was paid by the state to the holder of a purchase money mortgage upon which the petitioner was not personally liable. The remainder was paid to the petitioner who forthwith invested the amount received by him in similar property. Held that failure of the petitioner to invest in similar property the portion of the money which was paid to the mortgagee does not justify recognition of gain to

the petitioner. Fortee Properties, Inc., 19 T.C. 99, followed.

Tax on Real Estate—Assessment Prior to Acquisition by Petitioner—Real estate taxes assessed in March, and which became a lien at that time, held not deductible by petitioner who later in the year acquired title to the property and paid the taxes. Magruder v. Supplee, 316 U.S. 394.

AUSTIN CLAPP, ESQ.,
For the Petitioner.

J. EARL GARDNER, ESQ.,
For the Respondent.

Opinion

Atkins, Judge:

The respondent determined a deficiency in the petitioner's income tax for the calendar year 1949 in the amount of $15,323.09 and an addition thereto under section 293(a) of the Internal Revenue Code of 1939 in the amount of $992.38. The petitioner challenges only so much of the deficiency and addition as arises out of the respondent's determination that the petitioner realized a recognizable gain as the result of condemnation of real estate, and that the petitioner is not entitled to a deduction for an amount paid as real estate taxes.

The facts have been stipulated in full and are found as stipulated. A summary of the facts will suffice for the purpose of deciding the issues presented.

I. Gain on Condemnation Award

The petitioner timely filed his income tax return for the calendar year 1949 with the collector of internal revenue at Los Angeles, California.

In October, 1945, the petitioner purchased real estate known as the Elk Metropole Hotel in Los Angeles at a total cost of $89,600. At the time of purchase he executed a promissory note secured by a purchase money trust deed (sometimes referred to herein as "mortgage"), covering the land and building in the amount of $70,000. Principal and accrued interest on that note aggregating $57,572.63 remained unpaid on November 9, 1949. Interest paid by the petitioner on the note from October 1, 1945, to November 9, 1949, was claimed and allowed as a deduction from gross income in income tax returns filed during that period.

On November 9, 1949, the State of California, under condemnation proceedings, acquired the Elk Metropole Hotel, pursuant to a formal contract entered into between the petitioner and the State of California, which fixed the selling price at $207,323.34. On or about the same date, and in accordance with the contract,[1] the State of California

[1]The contract between the petitioner and the State provided that the State should pay the petitioner, as grantor, $207,323.34 for the property, payment to be made within 90 days after the date title vested in the State free and clear of all liens and encumbrances. However, it was further provided that, upon demand, any or all of the moneys up to

paid to the mortgagee of the property the sum of $57,572.63 representing the balance due on the trust deed note, and also paid directly to the petitioner the sum of $149,750.71, which payments aggregated the contract price of $207,323.34.

In March, 1950, an informal application to establish a replacement fund was made by the petitioner to the respondent. While this was pending, on July 7, 1950, the petitioner purchased the Sherwood Apartment Hotel in Los Angeles as a replacement of the Elk Metropole Hotel. The purchase price of the replacement property was $186,125 of which $149,750.71 was paid in cash by the petitioner from the moneys received from the State of California for the Elk Metropole Hotel property.

In his income tax returns for the years 1945 to 1949, inclusive, the petitioner claimed depreciation deductions in respect of the Elk Metropole Hotel in the aggregate amount of $8,166.66, of which the respondent allowed the amount of $8,000.

In his notice of deficiency the respondent held that since only $186,125 was expended by the petitioner for similar property, whereas the amount of

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and including the total amount of the unpaid principal and interest on the note secured by the deed of trust, together with any penalty for payment in full in advance of maturity, should be made payable to the beneficiary under the deed of trust, and that such beneficiary should furnish the grantor (the petitioner) with good and sufficient receipts showing such money credited against the indebtedness secured by the deed of trust.

the condemnation award was $207,323.34, gain is recognizable to the extent of the difference of $21,-198.34. He treated this as long-term gain and increased the reported taxable income by one-half that amount, or $10,599.17.

The substance of the petitioner's argument against the recognition of any gain arising out of the condemnation award is that his interest in the property and the interest of the mortgagee were several interests, that he sold only his interest, and that the amount he realized for his interest was fully reinvested in similar property; hence under section 112(f) of the 1939 Code there was no recognizable gain. The computation that he purposes on brief is as follows:

Down payment	$ 19,600.00
Payments on principal	12,427.37
Cost of interest sold	$ 32,027.37
Capital returned via depreciation	8,000.00
Basis of interest sold	$ 24,027.37
Gain realized	125,723.34
Total realized	$149,750.71
Reinvested	$149,750.71
Gain recognized	

Section 112(f) as it existed in 1949 provided as follows:

Involuntary Conversions—If property (as a result of its destruction in whole or in part, theft or seizure, or an exercise of the power of requisition or condemnation, or the threat or imminence thereof) is compulsorily or involuntarily converted into property similar or related in service or use to the property so converted, or into money which is forthwith in good faith, under regulations prescribed by the Commissioner with the approval of the Secretary, expended in the acquisition of other property similar or related in service or use to the property so converted, or in the acquisition of control of a corporation owning such other property, or in the establishment of a replacement fund, no gain or loss shall be recognized. If any part of the money is not so expended, the gain, if any, shall be recognized, but in an amount not in excess of the money which is not so expended.

Section 29.112(f)-1 of Regulations 111 provides in part as follows:

If, in a condemnation proceeding, the Government retains out of the award sufficient funds to satisfy liens (other than liens due to special assessments levied against the remaining portion of the plot or parcel of real estate affected for benefits accruing in connection with the condemnation) and mortgages against the property and itself pays the same, the amounts so retained shall not be de-

ducted from the gross award in determining the amount of the net award. * * *

In Fortee Properties, Inc., 19 T.C. 99, certain properties of the taxpayer were taken by the Port of New York Authority by condemnation under the power of eminent domain. Each of the properties was encumbered by mortgages which had been placed thereon prior to the time the taxpayer had acquired them. The taxpayer had not assumed the liability but had acquired the properties subject to the mortgages. The taxpayer and the Port of New York Authority agreed upon the total value of the properties. The Authority paid the amount due on the mortgages directly to the holder and paid the balance to the taxpayer. The taxpayer had no control over the payment or disposition of the amount paid in satisfaction of the mortgages. In that case it was held that the taxpayer, by investing the full amount of money which was paid directly to it, had complied with the provisions of section 112(f) and that it was not necessary to such compliance that it also expend in the acquisition of similar property an amount equal to the amount which was directly paid by the Port of New York Authority to the holder of the mortgages. It was pointed out that the taxpayer had not borrowed the money secured by the mortgages, did not receive directly, indirectly or constructively the amount necessary to satisfy the mortgages, and since it was not personally liable for the mortgage indebtedness, did not benefit by the payment of

such indebtedness. Certain cases were distinguished on the ground that therein money awarded was used by the Government to pay liens placed upon the property during the time it was owned by the taxpayer or to pay a debt for which the taxpayer was personally liable. In that case we stated in part:

> * * * If his (the Commissioner's) regulation is intended to cover a case like this one in which the petitioner was not personally liable for the mortgages, then to that extent the regulation is invalid because it frustrates rather than promotes the intention of Congress.
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> * * *
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> * * * The rather clear intention of Congress would be defeated rather than carried out if a part of the petitioner's gain were to be recognized because it did not also expend in the acquisition of similar property the $28,970 which it did not have invested in the condemned property, for the payment of which it was not personally liable, and which it did not receive directly, indirectly, or constructively. * * *

That case was reversed in Commissioner v. Fortee Properties, Inc., (C.A. 2, 1954) 211 F. 2d 915, cert. denied 348 U. S. 826. The Court of Appeals in holding in effect that the taxpayer had not complied with the requirements of section 112(f), took the view that, within the meaning of that section, the property sold was the full property and not merely the owner's rights over and above encumbrances,

and that the payment to the mortgagee, even though liability had not been assumed by the taxpayer, benefitted it. In so holding the Court of Appeals relied heavily upon Crane v. Commissioner 331 U.S. 1.

In our consideration of the Fortee case we gave thorough consideration to the Crane case and held that it had no application since it did not involve section 112(f) of the Code. In the Crane case the question presented was how a taxpayer, who acquired depreciable property subject to an unassumed mortgage, held it for a period, and finally sold it, still so encumbered, must compute the taxable gain. We were not concerned with any such question in the Fortee case. We were concerned with the question whether the taxpayer had invested in similar property all the money received upon the involuntary conversion of his former property so as to comply with the provisions of section 112(f). We have given careful consideration to the holding of the Court of Appeals for the Second Circuit in the Fortee case, but with all due respect to that court we adhere to the position taken by us in that case.

We have not overlooked the following statement contained in H. Rept. No. 798, 82nd Cong., 1st Sess., made in connection with Public Law 251, 82nd Cong., Act of Oct. 31, 1951, 65 Stat. 733, 1951-2 C.B. 353, which amended section 112(f):

> * * * A problem also arises under the present law where the taxpayer uses a part of the pro-

> ceeds from the converted property to pay off indebtedness on the converted property. In such a case the taxpayer is denied the benefits of section 112(f), that is, the taxpayer must pay a tax on any gain from the converted property up to the amount of the proceeds which are used in liquidation of indebtedness on the converted property, even though he also fully replaces the converted property, since the amount used to pay off the indebtedness cannot be directly traced into the replacement property.

In such a case as the instant case and the Fortee case, where an amount is paid to the mortgagee under a mortgage as to which the taxpayer has no personal liability, we think the money so used should not be considered as money received by the taxpayer. Cf. Kennebec Box & Lumber Co., Inc., v. Commissioner (C.A. 1), 168 F. 2d 646, and Ovider Realty Co. v. Commissioner (C.A. 4), 193 F. 2d 266, both affirming decisions of this Court.

There is no essential difference between the instate case and the Fortee case. The petitioner, under the condemnation procedure, entered into an agreement with the State of California fixing the amount of the award at $207,323.34, and the State of California directly paid off the mortgage indebtedness out of the $207,323.34. Here, although the mortgage was placed upon the property by the petitioner at the time of purchase, there was no personal liability

upon him for payment thereof, the mortgagee having recourse only against the property, in view of sections 580b and 580d of the California Code of Civil Procedure (West's Annotated California Codes, vol. 16, pp. 57 and 60),[2] as construed in Stone v. Lobsien, 112 Cal. App. 2d 750, 247 P. 2d

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[2]§ 580b. Purchase money mortgages, etc.; no deficiency judgment.

No deficiency judgment shall lie in any event after any sale of real property for failure of the purchaser to complete his contract of sale, or under a deed of trust, or mortgage, given to secure payment of the balance of the purchase price of real property.

Where both a chattel mortgage and a deed of trust or mortgage have been given to secure payment of the balance of the combined purchase price of both real and personal property, no deficiency judgment shall lie at any time under any one thereof. * * *

§ 580d. Foreclosure under power of sale; no deficiency judgment; exceptions:

No judgment shall be rendered for any deficiency upon a note secured by a deed of trust or mortgage upon real property hereafter executed in any case in which the real property has been sold by the mortgagee or trustee under power of sale contained in such mortgage or deed of trust.

The provisions of this section shall not apply to any deed of trust, mortgage or other lien given to secure the payment of bonds or other evidences of indebtedness authorized or permitted to be issued by the Commissioner of Corporations, or which is made by a public utility subject to the provisions of the Public Utilities Act. * * *

357, and Mortgage Guarantee Co. v. Sampsell, 51 Cal. App. 2d 180, 124 P. 2d 353[3].

We accordingly hold that the respondent erred in treating any part of the condemnation award as a recognizable gain.

II. Deductibility of Real Estate Taxes

On or about February 14, 1949, the petitioner entered into an escrow agreement for the purchase of certain real property in block 38, Hancock's Survey in the City and County of Los Angeles, California. On the first Monday in March, 1949, taxes were assessed in the name of the record owner, Fridi Seeber, against the property by the authorities of Los Angeles County. The terms of the escrow agreement were satisfied and settlement was made by the parties on April 4, 1949. In December, 1949, the petitioner paid taxes in the

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[3]In Stone v. Lobsien it was stated:

> * * * This was a purchase money deed of trust, and, in this state, there is no personal liability imposed on the vendee of a purchase money deed of trust. In the event of a default, no deficiency judgment could have been taken against appellant. § 580b, Code Civ. Proc.; * * *

In Mortgage Guarantee Co. v. Sampsell it was stated:

> * * * Section 580b, which is the section upon which appellant relies in this case, states, in effect, that there can be no deficiency judgment at all where property is sold under a purchase money mortgage or deed of trust. In other words, for a purchase money mortgage or deed of trust the security alone can be looked to for recovery of the debt. * * *

amount of $862.30 which had been assessed against the property on the first Monday in March, 1949, while in escrow. The petitioner in his income tax return for the calendar year 1949 claimed a deduction for such payment of $862.30. The respondent disallowed the deduction on the ground that these taxes were imposed upon the seller and that the payment by the petitioner constituted a capital expenditure.

In Magruder v. Supplee, 316 U.S. 394, the Supreme Court, in deciding whether a vendee of real property was entitled to deduct state and city real property taxes stated:

> * * * A tax lien is an encumbrance upon the land, and payment, subsequent to purchase, to discharge a pre-existing lien is no more the payment of a tax in any proper sense of the word than is a payment to discharge any other encumbrance, for instance a mortgage. * * *
>
> * * *
>
> Thus, either a pre-existing tax lien or personal liability for the taxes on the part of a vendor is sufficient to foreclose a subsequent purchaser, who pays the amount necessary to discharge the tax liability, from deducting such payment as a "tax paid." * * *

That case also establishes that in ascertaining the existence of either a personal liability for the tax on the part of a vendor or the existence of a lien

prior to the time of purchase thereof resort must be had to the law of the taxing authority.

The State of California Revenue and Taxation Code (West's Annotated California Codes, vol. 59, pp. 204, 334 and 341) provides in pertinent parts as follows:

§ 405. Annual assessment; time

Annually, the assessor shall assess all the taxable property in his county, except State assessed property, to the persons owning, claiming, possessing, or controlling it at 12 o'clock meridian of the first Monday in March. The assessor shall ascertain such property between the first Mondays in March and July. * * *

§ 2187. Tax on real estate; lien

Every tax on real property is a lien against the property assessed. * * *

§ 2192. Lien date

All tax liens attach annually as of noon on the first Monday in March preceding the fiscal year for which the taxes are levied. * * *

In view of these provisions of the statute it seems clear that the property taxes in question are those for the state's fiscal year ended June 30, 1950, but that a lien on account thereof attached to the property as of the first Monday in March, 1949. At that time the conditions of the escrow agreement had not been met and title to the property had not passed to the petitioner.

The petitioner first contends that the equitable owner of the property is personally liable for the tax and may be assessed for it, relying upon the case of First Trust & Savings Bank of Pasadena v. Los Angeles County, 206 Cal. 240, 273 Pac. 1066. The petitioner has cited no case, nor has any come to our attention, under which it could be considered that the petitioner obtained an equitable title to the property under the escrow agreement. Insofar as we can determine, neither equitable nor legal title passed from the original owner prior to the settlement on April 4, 1949.

The petitioner also contends that he should be considered as claiming and controlling the property on the first Monday in March, 1949, within the meaning of section 405 of the Revenue and Taxation Code quoted above. He has cited us no authority to support this contention and we have been unable to find any. Normally an escrow agreement, as we understand it, does not give the vendee control over the property or a claim to it prior to the satisfaction of the terms of the escrow.

We have held that under the laws of California the liability for property taxes is determined by the ownership of the property on the first Monday in March. California Sanitary Co., Ltd., 32 B.T.A. 122, Crown Zellerbach Corporation, 43 B.T.A. 541, Pacific Southwest Realty Co., 45 B.T.A. 426 (affirmed on other issues (C.A. 9), 128 F. 2d 815).

Here we think the petitioner was not, on the first Monday of March, 1949, the person owning,

claiming, possessing or controlling the property within the meaning of the California statute and that hence the taxes were not imposed upon him. Rather, we believe that when he did become the owner of the property it was impressed with a lien and that his discharge of such lien constituted a capital expenditure in the nature of additional cost of the land to him and that he is not entitled to deduct the amount of $862.30 as taxes paid, under section 23(c) of the Internal Revenue Code of 1939.

The respondent determined an addition to the tax under section 293(a) in the amount of $992.38. The petitioner does not allege error in the respondent's assertion of the addition, but does question the amount thereof. Section 293(a) provides:

> Negligence—If any part of any deficiency is due to negligence, or intentional disregard of rules and regulations but without intent to defraud, 5 per centum of the total amount of the deficiency (in addition to such deficiency) shall be assessed, collected, and paid in the same manner as if it were a deficiency, * * *.

The proper amount of the addition to tax will be fixed pursuant to the computation under Rule 50.

Decision will be entered under Rule 50.

Served: June 30, 1957.

Entered: June 30, 1957.

Tax Court of the United States

Docket No. 55993

FRANK W. BABCOCK,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

DECISION

Pursuant to the determination of the Court, as set forth in its Opinion filed June 28, 1957, the petitioner herein, on August 5, 1957, filed a recomputation for entry of decision, and the respondent herein, on August 23, 1957, filed a recomputation for entry of decision. The above recomputations are in agreement, and therefore, it is

Ordered and Decided: That there is a deficiency in income tax in the amount of $4,161.77 for the taxable year 1949, and additions to tax under section 293(a), Internal Revenue Code of 1939, in the amount of $727.40.

Entered: September 4, 1957.

[Seal] /s/ CRAIG S. ATKINS,
Judge.

Served: September 5, 1957.

Entered: September 5, 1957.

[Title of Tax Court and Cause.]

STIPULATION OF FACTS

It is stipulated that the following facts may be received in evidence without further proof; provided, however, that this stipulation shall be without prejudice to the right of either party to introduce other and further evidence not inconsistent with the facts stipulated; and provided, further that both parties to this stipulation reserve the right to object to the materiality and relevancy of any of the facts herein stipulated.

1. Petitioner Frank W. Babcock is an unmarried individual with residence at 501 South Los Angeles Street, Los Angeles, California. The petitioner filed his income tax return for the calendar year 1949 with the Collector of Internal Revenue at Los Angeles on March 15, 1950. Copy of the return is attached hereto as Exhibit 1-A.

2. On or about February 14, 1949, petitioner entered into an escrow agreement for the purchase of certain real property in Block 38, Hancock's Survey in the City and County of Los Angeles, State of California, as per map recorded in Book 7, pages 96 and 97, of Miscellaneous Records in the office of the County Recorder of said county and state. Copies of the escrow statement are attached as Exhibits 2-B and 3-C, respectively.

3. On the first Monday in March, 1949, taxes were assessed in the name of Fridi Seeber, the rec-

ord owner of the real property, against the said real property by the appropriate authorities of Los Angeles County, California. The escrow regarding the purchase and sale of the aforementioned property was to close on April 1, 1949, but did not close until April 4, 1949, as shown by the escrow instructions and statement, Exhibits 2-B and 3-C. Taxes were pro rated as of date of close of the escrow. (Exhibits 2-B, 3-C). In December, 1949, petitioner paid $862.30 of the taxes assessed against the real property on the first Monday in March, 1949, while in escrow. Petitioner claimed a deduction for such payment on his income tax return for the calendar year 1949, which deduction was disallowed by respondent.

4. On or about October 1, 1945, petitioner purchased real property known as the Elk Metropole Hotel located in the City of Los Angeles at a total cost of $89,600.00.

5. At the time of the purchase the petitioner executed a promissory note secured by a purchase money trust deed covering the land and the building in the sum of $70,000.00, of which $57,572.63, representing principal and accrued interest, remained unpaid as of November 9, 1949. Attached as Exhibit 4-D is a copy of the escrow instructions dated August 3, 1945.

6. Petitioner paid interest on the unpaid balance of said promissory note and trust deed from October 1, 1945, to November 9, 1949, which was

reported and allowed as a deduction from gross income in his income tax returns covering this period.

7. On November 9, 1949, the State of California, under condemnation proceedings, acquired said real property pursuant to a formal contract entered into between the petitioner and the State of California dated July 21, 1949, fixing the selling price at $207,323.34. Also, on or about November 9, 1949, and in accordance with the provisions of the contract dated July 21, 1949, the State of California paid the mortagee the balance due on the trust deed note of $57,572.63 and paid directly to the petitioner $149,750.71 for a total payment of $207,323.34. Attached as Exhibits 5-E and 6-F, respectively, are copies of the contract to purchase dated July 21, 1949, and the receipt retained by the State of California for the payment of $149,750.71 to Frank W. Babcock dated November 9, 1949.

8. Between November 9, 1949, and March, 1950, petitioner endeavored to find a suitable replacement property.

9. In early March, 1950, an informal application to establish a replacement fund was made by petitioner to the Commissioner of Internal Revenue, and while this was pending, a suitable replacement was found in the Sherwood Apartment Hotel, 431 South Grand Avenue, Los Angeles, California, which was purchased by petitioner for $186,125.00, of which $149,750.71 was paid in cash by the petitioner from the moneys received from the State

of California for the Elk Metropole property. The purchase of the Sherwood Apartment Hotel was made on or about July 7, 1950.

10. Section 580a, Code of Civil Procedure for the State of California provides in part as follows:

> "Whenever a money judgment is sought for the balance due on an obligation for the payment of which a deed of trust or mortgage with power of sale upon real property or any interest therein was given as security, the court may render judgment for not more than the amount by which the entire amount of the indebtedness due at the time of sale exceeded the fair market value of the real property or interest therein sold at the time of sale with interest thereon from the date of the sale; provided, however, that in no event shall the amount of said judgment, exclusive of interest after the date of sale, exceed the difference between the amount for which the property was sold and the entire amount of the indebtedness secured by said deed of trust or mortgage."

/s/ AUSTIN CLAPP,
Counsel for Petitioner.

/s/ JOHN POTTS BARNES, R.E.M.
Chief Counsel, Internal Revenue Service, Counsel for Respondent.

EXHIBIT 4-D

Escrow Instructions

Los Angeles, California
Escrow No. 2227-822-jj/jr
August 3, 1945

Title Insurance and Trust Company:

On or before Sept. 30, 1945, I will hand you the sum of $24,000.00, plus funds sufficient to cover my charges and prorations herein, together with the note and deed of trust for $70,000.00 set forth below, and the chattel mortgage, and I hand you herewith check for $1000.00, all of which you will deliver when you obtain and record for me a deed to vestee and covering property described below, and when you can issue your usual form—standard form—policy of title insurance with liability not exceeding $95,000.00 on all of Lot 2 and fractional Lots 1, 11 and 12 in Block 106, of the Bellevue Terrace Tract, in the City of and County of Los Angeles, State of California, being a Tract of land bounded as follows: On the North by the North line of said Lots 2 and 12 of said Block 106; on the East of Fremont Avenue and on the South and West by Sixth Street, as per map recorded in Book 2 Page 585 of Miscellaneous Records, showing title vested in Frank W. Babcock, an unmarried man.

Subject only to:

(1) All taxes for the fiscal year 1945-1946.

(2) Covenants, conditions, restrictions, and easements of record: (Subject to approval of buyer.)

(3) Deed of trust to file, any form, executed by vestee above, securing a note for $70,000.00, in favor of Call Estate Co., a corporation, with interest from date of note at 4½% per annum, principal and interest payable in installments of $535.00 or more per month, until paid, payable at Los Angeles, California.

Said trust deed to recite that it is given to secure a portion of the purchase price of the property in question.

Said note is also secured by a chattel mortgage on personal property, given as additional security therefor.

Pro rate as of date of close of escrow the following:

(a) Taxes based on second half taxes for 1944-1945.

(b) Insurance premium on policy or policies as handed you.

(c) Rents on 30-day basis, based on statement to be handed you, which statement is subject to my approval.

Do not draw note, trust deed or chattel mortgage. My execution of all of said documents will evidence my approval in full of all terms, contents and provisions thereof.

Endorse interest on above note as paid to date of close of escrow.

Also obtain for delivery to me at close of escrow without additional consideration, a bill of sale covering certain personal property on the premises in question, per inventory attached, which bill of sale and inventory I reserve the right to approve. No chattel search required. Title Insurance and Trust Company is liable only for the delivery of said document at close of escrow.

Also obtain for delivery to me at close of escrow the following leases, together with assignments of the seller's interest therein, which leases I reserve the right to approve:

(1) Lease in favor of Boris Pollack and assigned to Oscar Plotkin and Aaron Gordon; and

(2) Lease in favor of Harry Rasnick.

Deliver title insurance policy to beneficiary.

Instruct Recorder to mail deed to me; trust deed & chat. mtg. to beneficiary. I pay your buyer's service fee as charged; recording deed $1.00; mortagee's clause on ins. 25 cents each.

General Provisions

"All funds received in this escrow shall be deposited with other escrow funds in a general escrow account of Title Insurance and Trust Company with the Farmers and Merchants National Bank of Los Angeles. All disbursements shall be made by check of Title Insurance and Trust Company.

Recordation of any instruments delivered through this escrow, if necessary or proper in the issuance of the policy of title insurance called for, is authorized.

No examination or insurance as to the amount or payment of real or personal property taxes is required unless the real property tax is payable on or before the date of the policy of title insurance.

Execute on behalf of the parties hereto, form assignments of interest in any insurance policies (other than title insurance) called for herein and forward them upon close of escrow to the agent with the request, first, that insurer consent to such transfer or attach loss-payable clause or make such other additions or corrections as may have been specifically required herein, and second, that the agent thereafter forward such policies to the parties entitled to them. In all acts in this escrow relating to fire insurance, including adjustments, if any, you shall be fully protected in assuming that each such policy is in force and that the necessary premium therefor has been paid.

Time is of the essence of these instructions. If this escrow is not in condition to close by September 30, 1945, any party who then shall have fully complied with his instructions may, in writing, demand the return of his money and/or property; but if none have complied no demand for return thereof shall be recognized until five days after the escrow holder shall have mailed copies of such demand to all other parties at their respective addresses shown

in the escrow instructions. If no such demand is made close this escrow as soon as possible.

Any amendment of or supplement to any instructions must be in writing."

Buyer:

/s/ FRANK W. BABCOCK,
834 So. Main,
Los Angeles, California.

August 3, 1945.

Title Insurance and Trust Company:

I have read and approve the foregoing instructions. On or before September 30, 1945, I will hand you deed and bill of sale, together with the two leases and assignments, all as called for on page 1 hereof, which you will deliver when you can issue the policy of title insurance called for and collect for the account of the grantor the sum of $25,000.00, and obtain and record for the undersigned the note for $70,000.00 and deed of trust and chattel mortgage securing it as set forth on page 1 hereof.

Do not draw deed.

Pay at the close of escrow the sum of $4250.00 to N. M. Saunders, 1109 I. N Van Nuys Building, Los Angeles, California; License No. 17317, as commission and debit the account of the undersigned accordingly.

The foregoing General Provisions are hereby incorporated in these instructions.

Pay all incumbrances of record necessary to place title in the condition called for. I will hand you any funds and instruments required for such purpose.

Deliver title insurance policy to us.

Instruct recorder to mail trust deed & chat. mtg to us; deed to grantee.

Begin search of title at once. I pay policy fee and escrow fee, both as charged; recording deed of trust & chattle mortgage. Internal Revenue Stamps of $104.50, insurance transfers 25 cents each.

CALL ESTATE CO.

By /s/ [Indistinguishable.]

EXHIBIT "5-B"

FORM R.W.-1

Angeles California
ly 21, 1949

ACCT.	DIST.	COUNTY	ROUTE	SECTION	ALLOT.
	VII	LA	165	LA	7RV50

ANK W. BABCOCK,
unmarried man,
Grantor

Station to station

Side of Highway.

Rio Vista Subdivision
55 7295
C Par No. 14

RIGHT OF WAY CONTRACT—STATE HIGHWAY

Document No. 785 in the form of a Grant Deed

ring the following described property:

Lots 1, 2, 11 and 12 in Block 106 of the Bellevue Terrace Tract, as per map recorded in Book 2, Page 585, of Miscellaneous Records of Los Angeles County, as more fully described in above-mentioned Grant Deed,

APPROVED
JUL 30 1949
HQ. R/W OFFICE
BY

een executed and delivered to E. F. KING,

t of Way Agent of the State of California.

In consideration of which, and the other considerations hereinafter set forth, it is mutually agreed as follows:

1. The parties have herein set forth the whole of their agreement. The performance of this agreement constitutes otire consideration for said document and shall relieve the State of all further obligation or claims on this account, or on unt of the location, grade or construction of the proposed public improvement.

2. The State shall:

(A) Pay the undersigned grantor the sum of $207,323.34 for the property as conveyed by Grant Deed No. 785 within ety (90) days after date title to said property vests in the State e and clear of all liens, encumbrances, assessments and recorded /or unrecorded leasehold interests and easements except:

a. General and special City and County taxes for the fiscal year 1949-50, a lien not yet payable.

(B) Pay all escrow and recording fees incurred in this transaction, and, if title insurance is desired by the State, premium charged therefor. Said escrow and recording charges shall not, ever, include reconveyance fees, trustee's fees, or forwarding fees.

3. Any or all moneys payable under this contract, up to and including the total amount of unpaid principal and interest on the note secured by deed of trust recorded October 11, 1945 in Book 22244, Page 323, Official Records of Los Angeles County, together with penalty (if any) for payment in full in advance of maturity, shall, upon demand, be made payable to the beneficiary entitled thereunder; said beneficiary to furnish grantor with good and sufficient receipt showing said moneys credited against the indebtedness secured by said deed of trust.

4. All rents shall be pro-rated as of October 31, 1949. All rents derived from said property up to and including said date shall be paid to the grantor and all rents paid for occupancy after said date shall be paid to the State of California. If any rentals on said property have been or are collected by the undersigned grantor for any period beyond said date, the undersigned grantor for any period beyond said date, the undersigned grantor shall immediately refund such rentals to the State.

5. The undersigned grantor hereby agrees and consents to the dismissal of Parcel No. 14, People vs. Clare Schweitzer, Superior Court Case No. 557295, Los Angeles County, and also waives any and all claims to any money that may have been deposited in the Superior Court in said action.

6. Grantor hereby agrees to deliver up possession of premises now ~~non~~-occupied by him, i.e., Elk Hotel, 947-949 West Sixth Street; Metropole Hotel, 931-933 West Sixth Street; and rooming house, 941-943½ West Sixth Street by October 31, 1949 and, to that end, will immediately make application to the OPA for eviction of present tenants and take such other steps as will be necessary to deliver premises vacant on above date.

IN WITNESS WHEREOF, the parties have executed this agreement the day and year first above written.

Edward V. Patterson

C/O N. W. Saunders Co.
1109 I. N. Van Nuys Bldg.
~~834 South Main Street~~
Los Angeles, California

Grantor

Recommended for Approval,

Right of Way Agent

Recommended for Approval,

H W Leonard
Metropolitan District Right of Way Agent

STATE OF CALIFORNIA
DEPARTMENT OF PUBLIC WORKS
DIVISION OF HIGHWAYS

By G. D. Griffin
Asst District Engineer

No Obligation Other Than Those Set Forth Herein Will Be Recognized

EXHIBIT

EBT 508 3264 2-48 30M © OPO

EXHIBIT "6-F"

County: LA

Route: 165

Section: LA

Parcel No.: 785—Babcock

Received from the State of California, Dept. of Public Works, Division of Highways, Check No. Y78771, in the amount of $149,750.71, covering payment in accordance with Right of Way Contract dated July 21, 1949.

/s/ FRANK W. BABCOCK.

Dated at Los Angeles, California, November 9, 1949.

Filed at hearing January 10, 1957.

[Title of Tax Court and Cause.]

ADDITIONAL STIPULATION OF FACTS

It is stipulated that the following facts may be received in evidence without further proof; provided, however, that this stipulation shall be without prejudice to the right of either party to introduce other and further evidence not inconsistent with the facts stipulated; and provided, further

that both parties to this stipulation reserve the right to object to the materiality and relevancy of any of the facts herein stipulated.

11. Section 580b, Code of Civil Procedure for the State of California, provides as follows:

"No deficiency judgment shall lie in any event after any sale of real property for failure of the purchaser to complete his contract of sale or under a deed of trust, or mortgage, given to secure payment of the balance of the purchase price of real property.

"Where both a chattel mortgage and a deed of trust or mortgage have been given to secure payment of the balance of the combined purchase price of both real and personal property, no deficiency judgment shall lie at any time under any one thereof."

12. Section 580d, Code of Civil Procedure for the State of California, provides in part as follows:

"No judgment shall be rendered for any deficiency upon a note secured by a deed of trust or mortgage upon real property hereafter executed in any case in which the real property has been sold by the mortgagee or trustee under power of sale contained in such mortgage or deed of trust. * * *"

13. That the amount of depreciation claimed by petitioner in his federal income tax returns for the years 1945, 1946, 1947, 1948 and 1949 was the sum

of $8,166.66 of which the sum of $8,000.00 was allowed by Respondent.

/s/ AUSTIN CLAPP,
Counsel for Petitioner.

/s/ JOHN POTTS BARNES, R.E.M.
Chief Counsel, Internal Revenue Service, Counsel for Respondent.

Filed at hearing January 10, 1957.

In the United States Court of Appeals
for the Ninth Circuit

T. C. Docket No. 55993

COMMISSIONER OF INTERNAL REVENUE,
Petitioner on Review,

vs.

FRANK W. BABCOCK,
Respondent on Review.

PETITION FOR REVIEW

To the Honorable Judge of the United States Court of Appeals for the Ninth Circuit:

The Commissioner of Internal Revenue hereby petitions the United States Court of Appeals for the Ninth Circuit to review the decision entered by The Tax Court of the United States on September 4, 1957, ordering and deciding that there is a

deficiency in income tax in the amount of $4,161.77 for the taxable year 1949 and additions to tax under section 293(a), Internal Revenue Code of 1939, in the amount of $727.40. This petition for review is filed pursuant to the provisions of sections 7482 and 7483 of the Internal Revenue Code of 1954.

The respondent on review (hereinafter referred to as the taxpayer) resides at 501 S. Los Angeles Street, Los Angeles, California. The taxpayer filed his income tax return for the calendar year 1949 with the Collector of Internal Revenue at Los Angeles, California, and within the judicial circuit of the United States Court of Appeals for the Ninth Circuit, wherein this review is sought.

Nature of Controversy

The question involved is whether the gain of a taxpayer whose property is taken pursuant to condemnation proceedings is recognized to the extent of an amount retained by the Government and used to pay taxpayer's note secured by a mortgage against the property.

The substance of taxpayer's argument against the recognition of any gain arising out of the condemnation award is that his interest in the property and the interest of the mortgagee were several interests, that he sold only his interest, and that the amount he realized for his interest was fully reinvested in similar property; hence under section 112(f) of the 1939 Internal Revenue Code there was no recognizable gain.

The Commissioner took the position that the word "property" as used in section 112(f), relating to involuntary conversions, does not mean merely taxpayer's equitable interest, but also includes amounts used to pay taxpayer's note secured by a mortgage against the involuntarily converted property under section 29.112(f)-1 of Treasury Regulations 111 and Fortee Properties, Inc., v. Commissioner (C.A. 2, 1954) 211 F.2d 915; 45 A.F.T.R. 1347, with the result that the gain is recognizable to the extent of such amount.

/s/ CHARLES K. RICE, C.A.R.
Assistant Attorney General.

/s/ NELSON P. ROSE, C.A.R.
Chief Counsel, Internal Revenue Service, Counsel for Petitioner on Review.

Received and filed November 25, 1957, T.C.U.S

[Title of Court of Appeals and Cause.]

T. C. Docket No. 55993

STATEMENT OF POINTS

Comes Now the petitioner on review herein and makes this concise statement of points on which he intends to rely on the review herein, to wit:

The Tax Court of the United States erred:

1. In holding that failure of the taxpayer to invest in similar property the amount of money re-

tained by the Government in condemnation proceedings and used to pay taxpayer's note secured by a mortgage against the condemned property, did not justify recognition of gain to the taxpayer.

2. In failing to hold that taxpayer's failure to invest in similar property the amount of money retained by the Government in condemnation proceedings and used to pay taxpayer's note secured by a mortgage against the condemned property, rendered the gain taxable to the extent of such amount.

3. In holding that there is a deficiency in income tax for the year 1949 in the amount of $4,161.77 and additions to tax under section 293(a), Internal Revenue Code of 1939, in the amount of $727.40.

4. In failing to hold that there is a deficiency in income tax for the year 1949 in the amount of $15,323.09 and additions to tax under section 293(a), Internal Revenue Code of 1939, in the amount of $992.38.

5. In that its opinion and decision are contrary to law and regulations and are not supported by its finding of fact or substantial evidence.

/s/ CHARLES K. RICE, C.A.R.
Assistant Attorney General.

/s/ NELSON P. ROSE, C.A.R.
Chief Counsel, Internal Revenue Service, Counsel for Petitioner on Review.

Received and filed November 25, 1957, T.C.U.S.

[Title of Tax Court and Cause.]

CERTIFICATE

I, Howard P. Locke, Clerk of the Tax Court of the United States, do hereby certify that the foregoing documents, 1 to 12, inclusive, constitute and are all of the original papers on file in my office as called for by the "Designation of Contents of Record on Review," including joint exhibits 1-A thru 6-F, attached to the Stipulation of Facts, in the case before the Tax Court of the United States docketed at the above number and in which the Respondent in the Tax Court has filed a petition for review as above numbered and entitled, together with a true copy of the docket entries in said Tax Court case, as the same appear in the official docket in my office.

In testimony whereof, I hereunto set my hand and affix the seal of the Tax Court of the United States, at Washington, in the District of Columbia, this 10th day of February, 1958.

[Seal] /s/ HOWARD P. LOCKE,
Clerk, Tax Court of the
United States.

[Endorsed]: No. 15888. United States Court of Appeals for the Ninth Circuit. Commissioner of Internal Revenue, Petitioner, vs. Frank W. Babcock, Respondent. Transcript of the Record. Petition to Review a Decision of The Tax Court of the United States.

Filed: February 17, 1958.

/s/ PAUL P. O'BRIEN,
Clerk of the United States Court of Appeals for the Ninth Circuit.